SNC-Lavalin dodges questions on questionable spending as new CEO takes helm

By Nicolas Van Praet, Financial Post October 1, 2012

MONTRAL – SNC-Lavalin Group Inc., the Canadian engineering giant battered by a payments scandal that triggered criminal probes, declined to answer questions Monday about ongoing police investigations as a new report surfaced that executives with the company paid out money to help win a billion-dollar contract to build a new superhospital in Montreal.

In a 26-minute conference call designed to introduce SNC's newly chosen chief executive, industry veteran Robert Card, neither Mr. Card nor company chairman Gwyn Morgan would answer questions about anything related to current police probes. Mr. Card insisted he is settling in Montreal for a long period in an attempt to win back investor confidence.

The new chief executive disclosed that he is buying a home in Montreal, where SNC's headquarters are based, and has purchased roughly $1-million worth of SNC's common shares. Investors had been looking for a stock buy by the new CEO as a sign he has a stake in the game and that his interests are aligned with those of shareholders.

"I'm committed to ensuring that the company's social licence to operate remains our top priority," Mr. Card said on the conference call. "This includes ethics, health and safety, quality and related issues."
The comments came as Montreal's La Presse newspaper reported in its Monday edition that SNC-Lavalin executives are suspected of having made $22-million in questionable payments to win a huge construction contract to build the McGill University Health Centre's new megahospital.

Investigators with Quebec's police task force on corruption last month raided the centre's headquarters as well as those of Infrastructure Quebec, the government agency in charge of the project.

The newspaper report said the $22-million in payments were part of $56-million of funds uncovered by SNC-Lavalin earlier this year when it conducted an internal probe into undocumented payments to commercial agents. SNC has not disclosed which projects the payments were for and has not been able to track down the money. **Veritas Investment Research** has concluded that they are likely bribes.

The money was allegedly commissioned by Riadh Ben Aissa, former head of SNC's construction business, and approved by former CEO Pierre Duhaime.

Mr. Duhaime was let go with a sizable severance after the company said he had breached corporate policy. Mr. Ben Aissa was also let go and is now being held in a Swiss jail as part of that country's investigation into corruption, fraud and money laundering in North Africa. He was in charge of the MUHC project until recently.

La Presse's report is significant because it suggests that the unethical activities of certain individuals were not only taking place abroad, as previously believed, but also at home in Canada.

If proven, this information would almost certainly be damaging to the company's North American business. The company counts many governments among its customers, many of whom would think twice about doing business with a firm found guilty of paying bribes to win domestic contracts.

Asked Monday how much information it is sharing with current and potential clients about ongoing investigations, Mr. Morgan said the matter is in the hands of authorities.

"Other than what's public, we're not talking to investors or anyone else about it right now because there's a lot of things that we don't know ourselves. We're waiting to find out what the results of the investigations are."

La Presse's report states that the $22-million was not run through Canadian banks, but rather through several countries in 2010 and 2011. Made in U.S. dollars, the payments were made to a company that "appears fictional," the report says.

The McGill superhospital is one of Canada's largest public-private infrastructure projects, one lauded by industry for its structure and bond-financing. SNC is leading a consortium including British infrastructure investment group Innisfree Ltd. in financing and building the hospital. It will then lease the site to the Quebec government for 30 years.

Mr. Card is the first American to lead SNC-Lavalin in the company's 101-year history. He faces a shareholder base anxious for some finality to the current reputational scandals and for a new strategy that will help drive up the stock after a 22% fall this year.

Stephen Jarislowsky, the Montreal billionaire whose firm Jarislowsky Fraser Ltd. is one of SNC's largest shareholders, told Bloomberg News Mr. Card has to "clean house."

"A lot of people who were there who allowed [the ethics breach] to happen are still there," he said. "I wouldn't exactly be happy with somebody who signs cheques and didn't have the right explanation of what accounts this was for."

That view echoes that of **Veritas** Vice-President **Anthony Scilipoti**. In an April 26 report on SNC events titled "Skeletons in the closet," the Toronto-based analyst questioned whether the improper payments were isolated incidents and whether they're been contained. He said that as many as eight senior executives at SNC appear to have some knowledge of the improper acts committed even though only three of them – Mr. Duhaime, Mr. Ben Aissa, and former controller Stéphane Roy – have been formally cited by the company in connection with breaches of its ethics policies.

Mr. Scilipoti asks specifically why current chief financial officer Gilles Laramée was not asked to resign given that he failed to inform the company's auditors or any member of the board of directors of the impropriety even though he opposed it.

SNC Lavalin faces class action suits in both Quebec and Ontario over its alleged failure to disclose "all material facts" related to its international work. An Ontario judge has certified the action in that province after SNC declined to oppose the certification and the plaintiffs agreed not to seek punitive damages.

Monday marked Mr. Card's first day on the job as SNC's new chief executive and his remarks on the call were largely general and did not discuss the company's strategy going forward. Nevertheless, he said SNC's concession investments, including stakes in toll road Highway 407 and Calgary electricity transmitter Altalink, remain "a critical part" of the firm's strategy. Asked why he chose to join SNC-Lavalin when there are other companies also seeking executive talent, Mr. Card said the company has a strong capital base with "a lot more" potential than most firms to succeed in the long term.

"We've got to deliver" for stakeholders, Mr. Card said. "We've got to not have down-size surprises. We need up-side continuity. So that's what I'll be focused on."

Mr. Card has the right experience to manage SNC-Lavalin out of its current predicament, Altacorp Capital analyst Maxim Sytchev said in a research report to clients, noting his time leading CH2M Hill and work as under-secretary to the U.S. Department of Energy. "Despite the volatility around the name, SNC-Lavalin has a pristine balance sheet and strong concession portfolio that could be partially or fully monetized."

More importantly, said Mr. Sytchev, expectations for the company have been scaled down dramatically over the past six months, setting up a more "fertile ground" Mr. Card can build on. The analyst argues SNC-Lavalin might be the target of an activist investor eager to shake things up, much like Bill Ackman did at Canadian Pacific Railway Ltd.

In August, SNC lowered its profit forecast for the year to an expected maximum of $340-million, down from a previous prediction of $379-million.

Mr. Sytchev reaffirmed his "outperform" rating on SNC, and has a $50 price target on the shares.
SNC fell 2.5% to $37.00 in trading Monday morning on the Toronto Stock Exchange.